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A Supplement to
"Can Uncle Sam Do It Better?"

The Great Illusion

An Inexhaustible Public Purse

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the NAM Government Spending Committee

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April 1949
National Association of Manufacturers
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FOREWORD

This is a critical year for America's future. Government spending habits acquired during sixteen years of huge deficits are leading the American economy toward the kind of national crisis that has led other countries into various types of statism.

The American people, however, still have opportunity to choose among three courses: (1) taxes beyond what the traffic will bear; (2) new federal deficits and new inflation; and (3) sane, balanced federal budgets which will permit states and local governments to resume their rightful place in the American governmental pattern and permit the American economy to expand to its full potentialities of prosperity and national well-being.

This study is concerned primarily with only one aspect of the problem-federal grants-in-aid. These grants are not yet, in total, as large as some other major items of the federal budget. However, their postwar growth and their political implications make them worthy of the most serious attention by public officials and public-minded citizens.

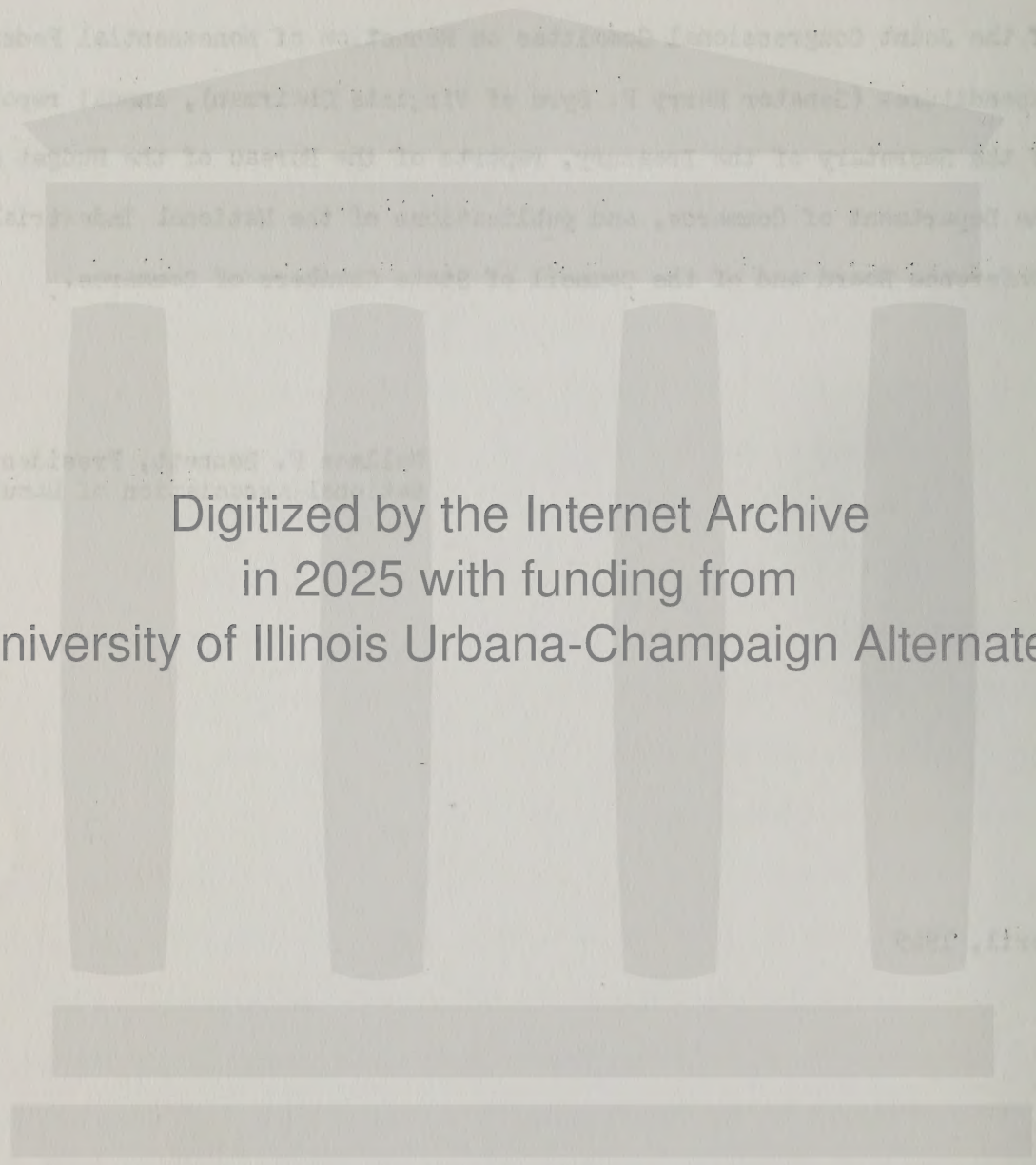
NAM's first report on federal grants-in-aid -- "Can Uncle Sam Do It Better?", published in January, 1948 -- received wide attention, required two reprintings. This second report, like the first one, was prepared by Thomas S. Holden, president of F. W. Dodge Corporation and chairman of the Federal Grants-in-Aid Subcommittee of the NAM Government Spending Committee, with the assistance of staff members of the Association's Government Finance Department.

Source material for this study was derived principally from the report

of the Joint Congressional Committee on Reduction of Nonessential Federal Expenditures (Senator Harry F. Byrd of Virginia Chairman), annual reports of the Secretary of the Treasury, reports of the Bureau of the Budget and the Department of Commerce, and publications of the National Industrial Conference Board and of the Council of State Chambers of Commerce.

Wallace F. Bennett, President
National Association of Manufacturers

April, 1949



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THE GREAT ILLUSION

This is the Great Illusion: The belief that the federal government's resources are inexhaustible and free. From 1930 through 1946, the federal government spent more than it took in for several reasons: a) necessity, as in financing the recent World War; b) a vain effort to promote recovery, as in the 1930's; and c) misguided paternalism, as in the grants, subsidies, and other hand-outs so lavishly distributed. Chart I shows the amounts spent by methods of financing. One sinister product of this long record of the government spending more than its income is the belief that its resources are inexhaustible.

In the present report, emphasis will be laid upon only one of the ways in which we as a people are proceeding as if there were no limit to government's ability to hand out money, namely, grants-in-aid.

The term "grants-in-aid" means the support given by one governmental unit to another, as federal grants to the states and state grants to the cities.

Another form of giving away public money is the "subsidy", which means the payments made by government to individuals, groups of individuals, and non-governmental beneficiaries generally. This report deals only with federal grants-in-aid, which have been made chiefly to the states, although some grants were made directly to cities and other local units during the 1930's. There are indications that pressures are developing to revive this practice.

Revival of Local Grants Movement

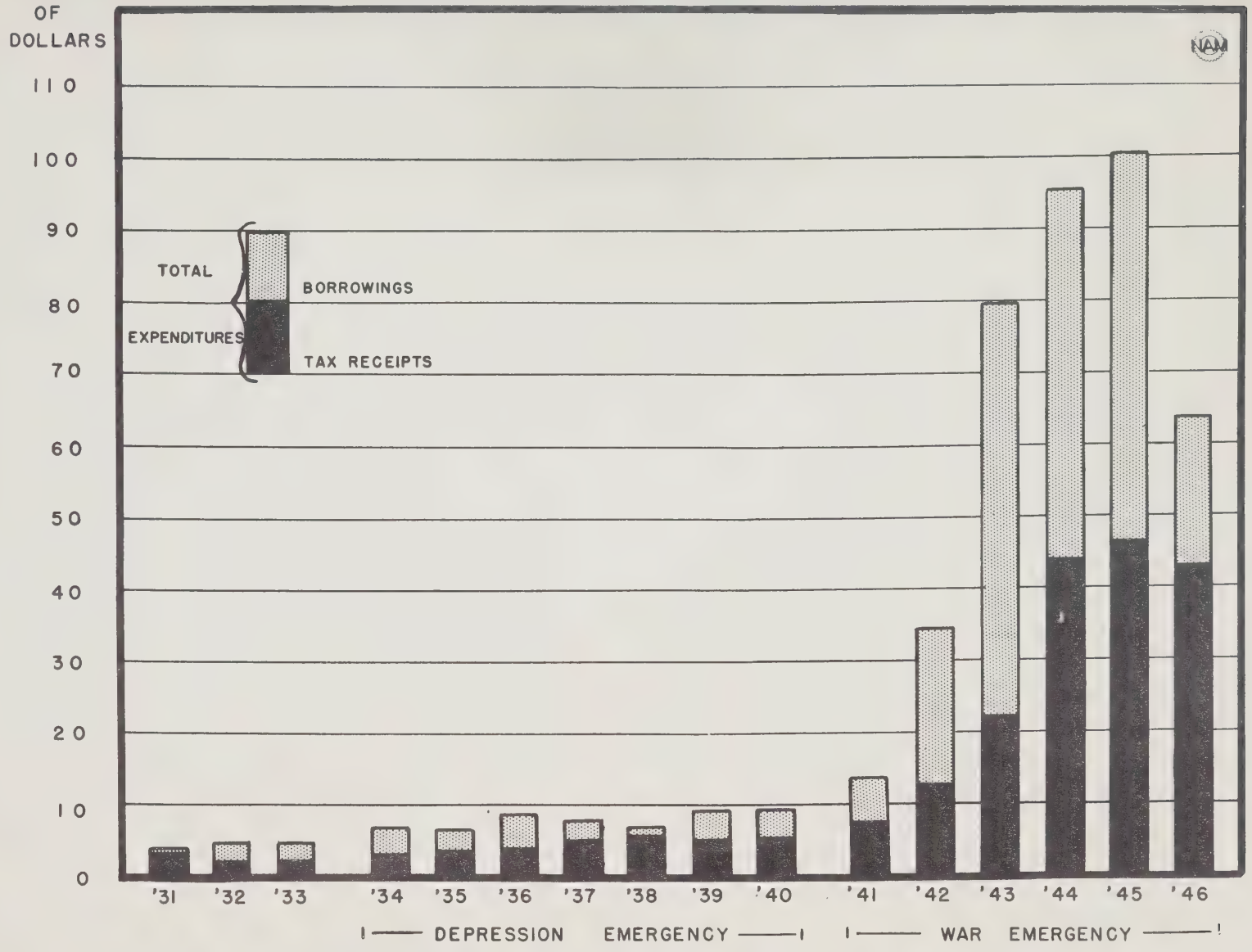
The readiness of states and cities to accept federal grants indicates a willingness to live in a world of illusion rather than reality. It implies that the federal government has resources outside those available to state and local governments, that federall money is free.

Allice-in-Wonderland

Chart 1

FEDERAL EXPENDITURES BY SOURCE OF FUNDS

1931 — 1946



SOURCE: ANNUAL REPORT OF THE SECRETARY OF THE TREASURY — 1948

Grants Demoralize Everyone

Hard-headed state and local officials really know better than this, and some of them would prefer to meet their responsibilities without federal aid. But any grant or hand-out program promptly demoralizes everyone because of the urge for each to get a share of the hand-out for his community, since the money is available and will be spent anyway.

Same People Support All Government

Actually, all governments, federal, state and local, must be supported by the wealth and income of the same people. The federal government has no resources other than these, and every dollar that it gives or offers to give must be taken from someone else. All kinds of government can obtain funds by borrowing, but as long as we adhere to the principle that public debts shall be honored by repayment, the money for debt redemption must be taken from the pockets of the people.

The illusion that federal money is easy and relatively costless money has been fostered by the notion that someone else, usually the well-to-do, pay all of the taxes.

High Incomes Can't Carry Load

It may be possible to concentrate tax burdens on the wealthy when governmental costs are low. But we have long since passed the point in this country at which these costs can be laid on one small group. The annual tax revenues of federal, state and local governments are approaching $60 billion, which is about 25 percent of current net national product. Spending programs are under consideration which, if adopted, would send the tax collections still higher. And the plain fact is that there just is not enough income in the middle and higher income classes to provide this much money, even if all of it were taken.

For example, there are some 174,000 persons with net incomes of $25,000 and more, and the total net income (income after deductions but before exemptions) was estimated to be $9.5 billion in 1948. At the 1948 tax rates it was estimated that the federal taxes on this income would be $4.7 billion. If the whole of the tax increase of $4 billion proposed by

the President were to be imposed on the persons with net incomes of $25,000 and more, there would remain for all personal and living expenses, and saving and investment, only $800 million out of the original $9.5 billion, or an average of $4,600 per taxpayer in the group.

It would not be practical to provide all of the money which the federal government is now taking in individual income taxes from the net incomes of $5,000 and over. In the calendar year 1948, the individual income tax collections were $20,281 million, before a final accounting for refunds. The 1948 total of net incomes of $5,000 and over is estimated at $28,695 million. The number of taxpayers in these net income classes was estimated to be 2,415,300. Assuming that the individual refunds on 1948 collections will be as much as $2 billion, there would remain a total of $10,434 million if the entire amount of the 1948 income tax had been imposed on net incomes of $5,000 and more. This would leave, for all personal and living expenses, and saving and investment, an average of $4,300 per taxpayer in the $5,000 and over group.

The effect on the economy of this kind of drastic leveling down needs no emphasis. The federal tax law, fortunately, does not go that far.

Lower Incomes Must Bear Share

Actually, there is now paid, out of the net incomes under $5,000, a somewhat larger share of the total individual income tax than is derived from the net incomes above that amount. This results from the immense proportion of the total taxable income that falls into the lowest net income brackets. For 1948, it was estimated that there would be approximately $110 billion of net income in net income classes up to $5,000. With the present demand for revenue, it is impossible to avoid levying upon this part of individual income.

In fact, it is possible to go farther and say that even the people

Everyone Pays

whose incomes are so small that they do not pay income taxes are paying heavy taxes of various sorts, directly or indirectly. In these days when

every business, large or small, is a tax collector for the government, no one escapes the eagle eye or the grasping hand of the Bureau of Internal Revenue. Corporations which are taxed must recover the taxes they pay, either from their customers or from their owners (stockholders) -- and stockholders are people, the vast majority of them people of moderate means. There is no escape from the conclusion that, in relation to his income and wealth, every citizen bears a significant part of the cost of government including the servicing and retirement of debt resulting from deficit financing.

CONCENTRATION OF FISCAL AND ADMINISTRATIVE POWER

The illusion that the federal resources are limitless has furthered the growth of federal power and corresponding deterioration of the autonomy, independence and constitutional authority of the states. Important as the purely financial aspects of the grants-in-aid program are in terms of total cost and their extravagance and waste, their tendency to alter the structure of American government is even more important.

Concentration of taxing power spells concentration of authority. Concentration of spending power spells concentration of patronage. As was seen in the deficit era, spending power may not always be limited by tax revenues.

Concentration of Government Greatest Threat

Concentration of spending power and of patronage has resulted in a dilution of the authority of the states and a tendency toward dependence of local governments on the federal treasury, contrary to the governmental philosophy embodied in the constitutions of the United States and of the forty-eight states. These days much concern is expressed over concentrations of economic power which are supposed to threaten the well-being of small businesses; much less concern is shown over actual concentration

of political power which threatens virtual extinction of our smaller units of government. This tendency toward monopoly in the governmental sphere is the great menace to preservation of American freedoms.

The newly concentrated power is not retained by Congress, the people's representatives, but is delivered over to federal administrative officials. A number of federal agencies have developed powerful lobbies, powerful propaganda machines, and powerful pressure group support for their programs. Some have scores or even hundreds of regional and local offices, thousands of employees. Among them are many engaged in political activities, even beyond the limits of the law.

Federal Administrators Exercise the Power

From time to time much evidence has been presented before Congressional committees of the use of relief and public work grants for purposes of influencing presidential and congressional elections.

Undue concentration of taxing and spending power constitutes an erosion of American freedom. It follows the European, not the American pattern. There is little evidence that its full significance is realized by the majority of American voters.

Partly from lack of public understanding, partly from inadequate resistance to pressure groups, the United States is moving steadily toward collectivism. It has an enormous debt, peacetime conscription, a vast and growing military establishment, an extreme centralization of fiscal and political power, a social security system which provides the government with a current spending fund and daily enlarges the government's obligations to millions of individuals. It faces the early possibility of unbalanced budgets.

Movement toward Collectivism

That is the pattern that has been followed with minor variations in practically every civilized country ever since Count Bismarck invented it as the favored instrument for prussianizing Germany. It has nowhere been

successful in providing genuine economic and social security; it has invariably led to national insolvency or totalitarianism or both.

United States Has No Excuse

Of all the countries of the world, the United States has the least excuse for following that pattern. The only way to escape its consequences is to dispel the illusion that government, as such, is a source of security, prosperity, and wealth. These things come only from the industry, initiative, and thrift of the people. We can have as much well-being and social gain as we are willing to work for and produce. Government can and should maintain the conditions of order and security, abroad and at home, under which the people are able to produce most abundantly. Since all taxation is burdensome, the process of imposing excessive taxes on one section or group in order to distribute benefits to another section or group is a net drain on the whole economy. It impairs the capacity and incentive of the over-burdened taxpayers to produce, while it induces in the beneficiaries a pleasant sense that good things can be had without too great effort.

The two major arguments used to promote federal grants-in-aid are these:

I. If we can afford X billions for this purpose, we can afford Y millions for grants to the states;

II. The "poorer" states need federal aid.

IF WE CAN AFFORD THIS, WE CAN AFFORD THAT.

Befogged Thinking

It is a specious, and dompletely fallacious argument to say that because we are spending heavily for one purpose, therefore we are able to spend for some other purpose. Such thinking is befogged by the great illusion that federal resources are inexhaustible. It assumes, apparently that the large amounts spent for such functions as the military

establishment and the foreign aid program, for example, are well within our capacity to carry, in other words that these things are being done because we can very well afford to do them. And it evidently proceeds to the assumption that because these very large items appear to be well within our capacity, therefore we can also afford a few hundred millions for an educational aid grant, or a public housing grant, or some other kind of grant to the states.

Military-Foreign Aid Programs Heavy Burdens

The fact is that a large military budget and a large foreign aid program are not being carried today because they are the kind of thing that a rich nation can afford, as a symbol of the national ego and a demonstration of the national generosity. On the contrary, the amounts that are being spent for these purposes today involve a heavy drain on the economy and a serious strain on the resources of taxpayers. The only justification for them, in their present amounts, is sheer, stark necessity, a kind of heavy insurance premium paid to underwrite peace in the future. In a very significant sense we cannot afford them, and the only justification for making them is that the calculated risks appear to be less costly than other lines of action.

Other Things Can not be Afforded Now

It is, therefore, nonsense to speak of our military and foreign aid expenditures as if they were outgos well within our means. The plain fact is that just because the decisions leading to the present and prospective costs of these programs have been made, there are many other purposes for which we simply cannot afford now to spend money. It is all the more necessary, in order to preserve the economic strength and soundness of the economy, and to avoid tax burdens that will seriously weaken it, to declare that these other things cannot be afforded now, regardless of any intrinsic merit which they may have. This position should be taken, too, regardless of the popular pressure and demand that

may have been generated, for it has been the foolish insistence upon affording this because, seemingly, we can afford that, which has underlain much of the pressure for the grants.

SHOULD UNCLE SAM HELP THE "POORER STATES"?

The Leveling Process

It is obvious that variations exist among the states in wealth and income-producing capacity, just as there are differences in soil and climate. An insidious application of the great illusion is that the federal government should use its fiscal powers to equalize economic and social conditions among the states. Specifically, this involves a leveling process by which federal taxation is to be used to transfer the fruits of economic effort from certain states to other states, in the form of federal grants.

States are Sovereign Entities

The particular territorial division of continental United States into the areas which we now identify as the forty-eight states is the result of a series of historical accidents. Whether or not the boundaries that were originally established are identical with those which would now be set up if it were possible to re-cast the pattern is beside the point. We do have forty-eight states as an accomplished fact, and we have a constitution under which each state is recognized as a sovereign entity, having substantial powers and responsibilities.

Taxation Perils "Poor" as well as "Rich" States

It was said above that the effect of our ever-expanding grants-in-aid system, together with the rising load of federal taxation required to carry these grants, threatens the integrity of our American system. If this be so, how can the so-called "poor states" really be permanently helped by such a program? If the American system itself is in peril, the poor states are in the same jeopardy as the rich states.

Issues Posed

Two vital issues are involved. The first is the extent to which a case exists for the kinds of leveling that current and proposed grant-in-aid programs would impose. The second, which goes far beyond the scope and implications of grants-in-aid, is the proper kind of program whereby all of the states, regardless of their present economic status and prospects, can develop the capacity at home to discharge responsibilities which are properly theirs, but which it is now assumed they can meet only by the legerdermain of federal aids.

Uniformity the Goal

In support of the current type of grant-in-aid program, it is argued that some states are unable to provide minimum standards of certain services from their own resources. The proposed policy assumes that uniform standards and procedures are desirable throughout the country and that the best people to determine the standards and procedures are federal administrators and their pressure-group allies. There is no evidence that the administrations, legislatures or the people of the so-called poorer states demand this kind of aid. There is, however, in many of the states a growing tide of opposition to the idea of extending grants-in-aid.

Coercion the Instrument

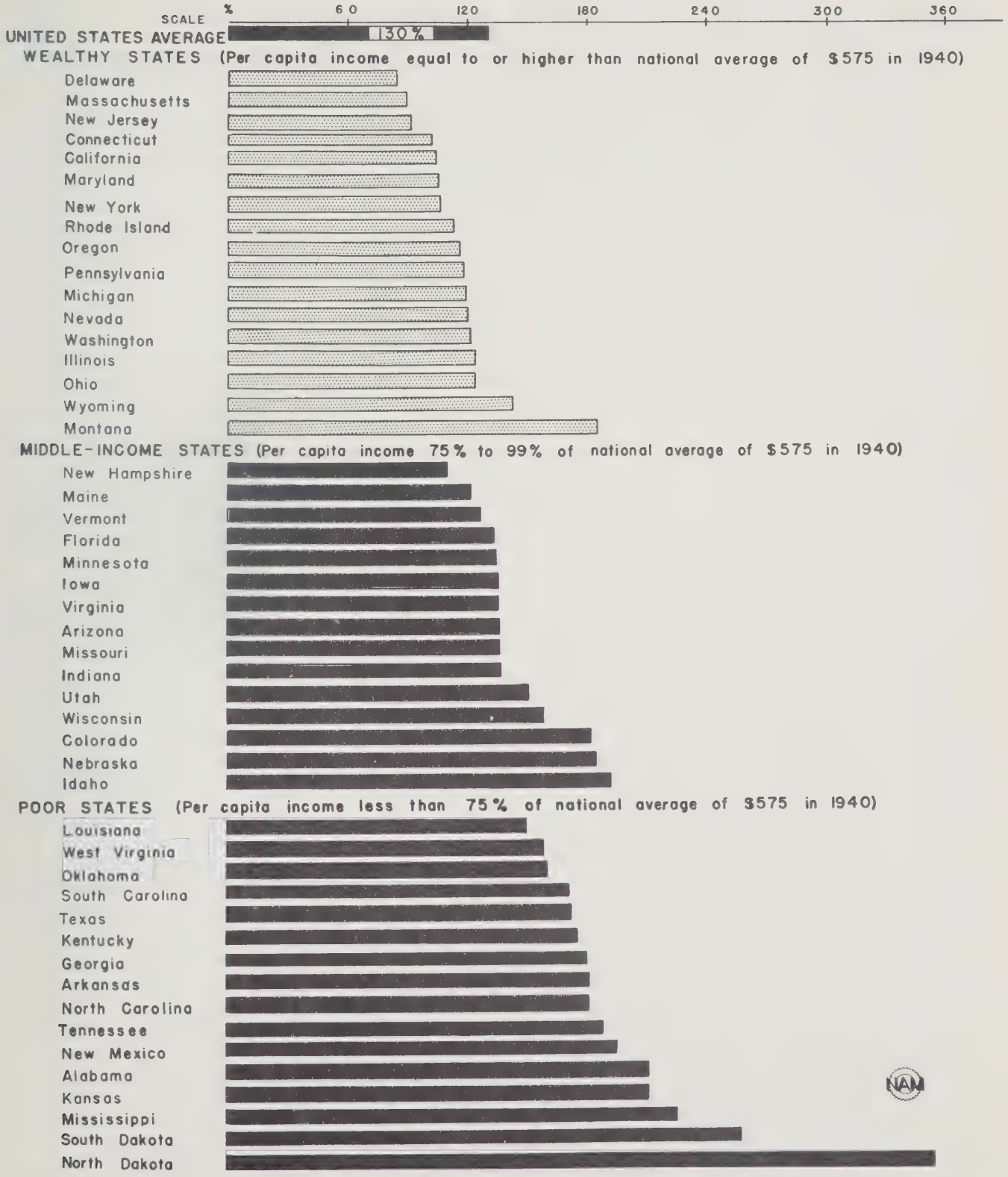
The proposed new policy substitutes for the prevailing concept of grants-in-aid as "cooperative arrangements", a concept of coercion -- coercion upon the more prosperous states to support the institutions of other states, coercion upon the "poorer states" in meeting standards to be imposed upon them from outside.

Actually, the relative status of the states in terms of incomes produced is subject to rapid change in our fluid, dynamic economy. This is well illustrated in Chart II and the table attached as Appendix A, which show how well the so-called poorer states fared in per capita income increases from 1940 to 1947.

Chart II

PERCENTAGE INCREASE IN PER CAPITA INCOME BY STATES

1940 – 1947



Source: Reports of the U.S. Department of Commerce

Economic Forces Increase Income

Industrialization, agricultural diversification and development of natural resources are improving the condition of the poorer states more than any system of doles charged against taxpayers in other sections of the country. Federal programs appropriately devised to accomplish such developmental purposes, coupled with removal of any existing inequities which may hamper the development of particular states or regions, are the kinds suitable for a free, dynamic economy. Such programs increase the total wealth of the nation.

Actually, the standards and the necessary costs vary considerably in various sections of the country, and little is to be gained by trying to make them uniform.

States Should Experiment

A great advantage of our federal system has been the opportunity for the states to experiment in social legislation. Under our present growing centralization, the whole nation becomes the guinea-pig, and experiments are conducted on the national scale by remote control.

COST OF AID PROGRAMS

Education Aid Realities

In floor debate on the Federal Aid to Education bill, Senator Irving M. Ives, of New York, who favored the proposal, estimated that it would cost his state $60,000,000 and return to it $12,000,000 in benefits. Nevertheless, the spell of the great illusion leads many New Yorkers to look upon this bill as indispensable to their schools. Governor Driscoll of New Jersey stated it would cost the taxpayers of his state $11,000,000 and return them only $4,000,000. Preserving the illusion is a costly business in these states.

Opposition to Federal Aid

Governor Driscoll, however, is strong in his denouncement of the bill. He is one of the most outspoken opponents of federal aid among the governors. "New Jersey", he has stated, "has consistently taken the position that it wants to do more and more for itself while asking the

federal government to do less and less."

Governor Driscoll's state ranks sixth in terms of per capita income. Virginia ranks thirty-first, is not likely to be heavily taxed for contributions to other states. Yet here is what Governor William M. Tuck of that state, wrote on the general subject of federal grants, in the October, 1948, issue of "Tax Outlook":

> "All the funds the federal government ever had, or ever will have, came from the taxpayers of the various states. Whatever the federal government allocates to the states comes from the people. Before this tax money comes back to the states and localities in the form of grants-in-aid, substantial tolls are exacted from it to maintain and enlarge the bureaucratic central agencies. Furthermore, citizens of such states as Virginia in this way ship a disproportionate part of their tax resources to Washington for the support of federal-aid programs in other states, where less efficient governments call for greater and greater federal dispensations."

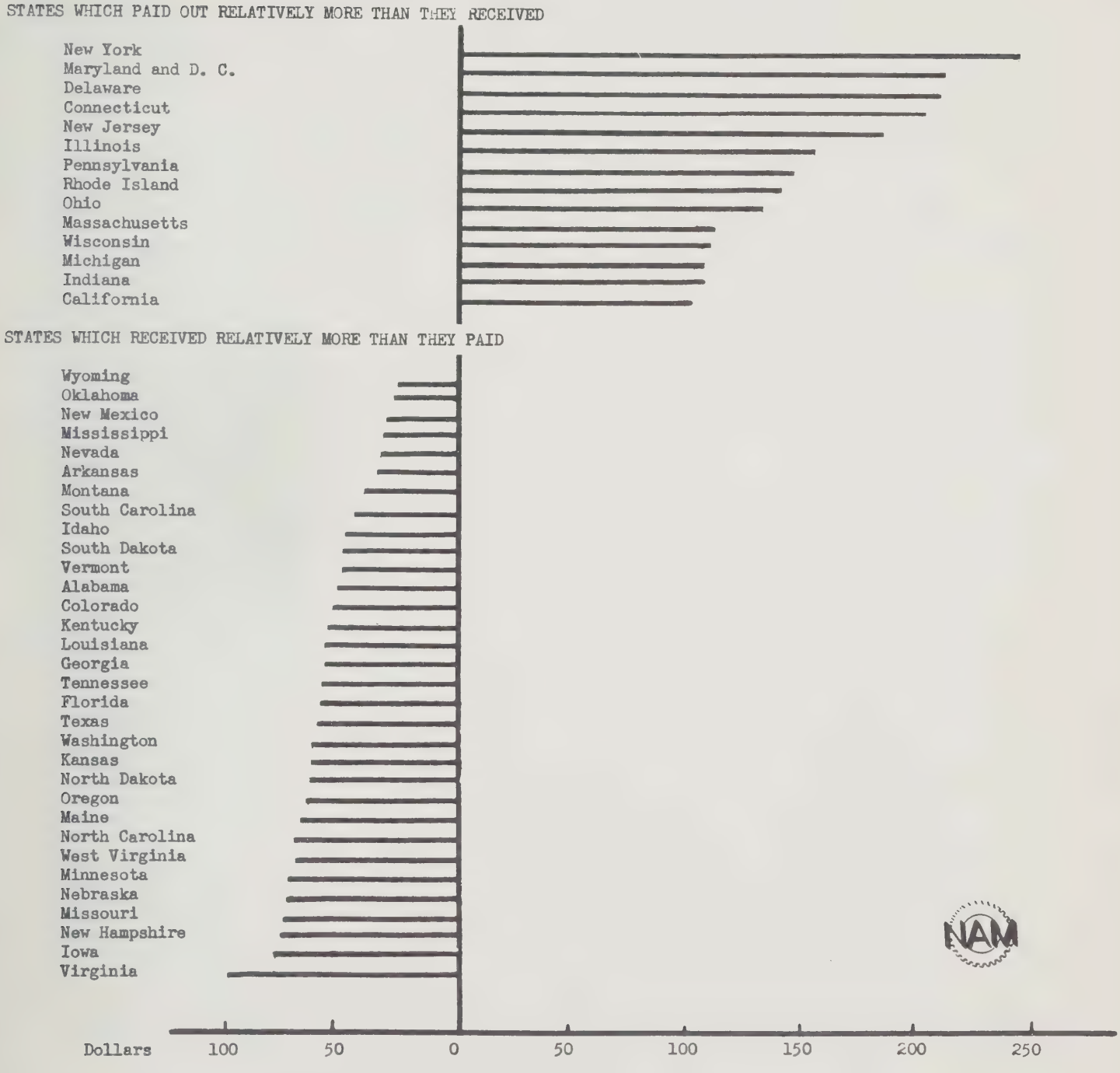
Transfer of Income by Grants

The transfer of income from some states to others by the combination of federal taxes and federal grants is shown in Table I and Chart III. This table shows, for the fiscal year 1948, the amount paid by the citizens of each state out of every $100 of federal taxes collected in that year, excluding the payroll taxes; and it also shows the amount received by each state out of every $100 of federal direct grants. It is recognized that no precise method can be devised which would produce an absolutely accurate distribution of federal taxes among the citizens of the several states. In this table, the individual income taxes are deemed to be paid by the citizens of the states according to the reported collections, and no allocation was made. The corporation taxes, customs, excises and miscellaneous taxes are distributed among the states according to income payments. The direct grants to the states were reported in the annual report of the Secretary of the Treasury for the Fiscal Year 1948.

Chart III

COST TO THE STATES OF $100 IN FEDERAL GRANTS

In 1948



Source: Prepared from reports of the Department of Commerce and United States Treasury

TABLE I

Amounts contributed by the States to every $100 of Federal taxes collected, and received by States of every $100 of Federal grants in 1948.1/

State	State's Tax Quota in each $100 of Federal Collections	State's Share in each $100 of Federal Grants	Cost to State of $100 in Grants
Part 1			
States which paid out relatively more than they received			
California	$ 8.72	$ 8.61	$101.28
Connecticut	1.79	.88	203.52
Delaware	.43	.20	215.00
Illinois	8.09	5.24	154.38
Indiana	2.27	2.16	105.09
Maryland & D.C.	2.90	1.34	216.41
Massachusetts	3.50	3.01	116.27
Michigan	4.75	4.20	113.09
New Jersey	3.43	1.86	184.41
New York	16.11	6.62	243.35
Ohio	5.88	4.43	132.73
Pennsylvania	7.66	5.26	145.62
Rhode Island	.60	.43	140.00
Wisconsin	2.10	1.83	114.75
Part 2			
States which received relatively more than they paid			
Alabama	.98	1.89	51.85
Arizona	.34	.83	40.96
Arkansas	.52	1.49	34.90
Colorado	.85	1.58	53.80
Florida	1.27	2.16	58.79
Georgia	1.28	2.24	57.14
Idaho	.33	.68	48.53
Iowa	1.50	1.91	78.54
Kansas	1.15	1.83	62.84
Kentucky	1.01	1.84	54.90
Louisiana	1.02	1.79	57.00
Maine	.41	.61	67.21
Minnesota	1.77	2.46	71.95
Mississippi	.50	1.56	32.05
Missouri	2.51	3.41	73.60
Montana	.34	.83	40.96
Nebraska	.83	1.15	72.17
Nevada	.12	.35	34.28
New Hampshire	.27	.36	75.00

New Mexico	.25	.81	30.86
North Carolina	1.38	2.00	69.00
North Dakota	.38	.60	63.33
Oklahoma	.98	3.41	28.77
Oregon	1.01	1.59	63.52
South Carolina	.62	1.39	44.60
South Dakota	.34	.68	50.00
Tennessee	1.22	2.11	57.82
Texas	3.93	6.62	60.00
Utah	.33	.81	40.74
Vermont	.17	.34	50.00
Virginia	1.38	1.41	97.87
Washington	1.68	2.72	61.72
West Virginia	.81	1.17	69.22
Wyoming	.17	.65	26.15

1/ The method of determining the relative state shares of taxes and grants was as follows:

The total of corporation taxes, excise and miscellaneous taxes, and customs receipts for the fiscal year 1948 was distributed among the states according to the income payments to individuals in 1947. To the amounts of these taxes, as so allocated, were added the actual collections of individual income tax in each state, and the share which each state contributed to the total taxes was computed as a percentage. The total of federal direct grants to the states in the fiscal year 1948 was likewise computed as a percentage of the total. Obviously, the amounts shown in this table are percentages converted into the part of $100 of taxes, or of grants, paid or received by the respective states.

Some States Lose

In Table I, the relationship between each state's relative share of taxes and grants, respectively, has been expressed, in the last column, as the cost to the state of $100 in grants. The figures make it perfectly clear that the federal grant system is a losing proposition for the fourteen states in Part 1 of the table, and of comparatively small advantage to some of the states in Part 2, notably, Iowa, Missouri, New Hampshire, and Virginia. The fourteen states which are now paying such heavy premiums to get some of their tax money back in the form of grants would be better off if the grant formulas were set up so as to hand out money only to the demonstrably indigent states, and to assure a corresponding reduction of the federal taxes. For some curious reason, it has always been assumed that every state must share in the grant in order to get that state's political support for the grant system. The data in Table II make it perfectly plain that every one of the fourteen states that were on the short end of the tax-grant combination in 1948 could have done, for itself, everything that was done under the grant system at less cost than it had to bear under the existing grant program.

Overhead Costs Additional

In addition to the sums of money distributed among the states, there is also the overhead cost of maintaining the federal agencies which administer grants-in-aid programs. Since a number of federal agencies administering grants-in-aid programs maintain regional, state, and even local offices, with large personnel, office, and travel expenses, the overhead cost can run into quite large figures. Senator Harry F. Byrd, of Virginia, has estimated the average overhead cost of giving away federal money at 15 percent. Whatever the overhead cost of a particular grants-in-aid program may run to, it will be added to

the taxes which the residents of the several states must pay into the federal treasury.

In terms of aggregates, the taxes collected and the grants paid were distributed as follows in 1948 between the two groups of states:

	Taxes		Grants	
	Amount (000)	%	Amount (000)	%
14 states in Part 1, Table I	$27,175,857	68.3	$ 729,798	46.1
34 states in Part 2, Table I	12,601,318	31.7	848,832	53.9
Totals	$39,777,175	100.0	$1,578,540	100.0

Since the fourteen relatively rich states paid 68.3 percent of the taxes in 1948, they, therefore, contributed this proportion of the federal grants, or $1,078,143,000. They received back out of their own money, $729,708,000. Hence, they contributed to the other states a total of $348,434,000, aside from the overhead costs of administering the various grants. Collectively, they would have been better off in 1948, if federal taxes had been lower by the amount of the grants which they received out of their own funds and if the grant system had been limited to the definitely poor states. Had such a procedure been in operation, there would have been a much closer scrutiny of the purposes of the grants and no doubt an elimination of many trifling expenditures, the main result of which has been to extend as widely as possible the area of federal control and supervision of local affairs.

FEDERAL VERSUS STATE AND LOCAL TAXES

Squeezing Tax Resources

One of the most serious consequences of excessive and unnecessary Federal spending for grants-in-aid and other purposes is the difficulty created for state and local governments to meet their own budget requirements out of tax resources remaining to them.

A striking example is furnished by a survey of all taxes paid by the people and enterprises of Montgomery County, Ohio, in the year 1947.

That is the county of which Dayton, a prosperous industrial community, is the principal city. The following report on the Montgomery County tax study is quoted from the National City Bank of New York's Monthly Letter on Economic Conditions and Government Finance (December, 1948, issue):

> "* * *Total tax collections from all sources in Montgomery County amounted to more than $216,000,000, which, on the basis of a 375,000 population, means an average of approximately $578.00 tax collections per person. Of this total tax take, the Federal Government got the lion's share, with 81 per cent. The State of Ohio came a poor second with 11 per cent; with the local governments (City of Dayton, Montgomery County, Dayton School District) trailing still further behind with only 8 per cent."

Urban Areas Fare Poorly

The Montgomery County tax pie was sliced 81 percent federal, 11 percent state, 8 percent local. The national tax pie that year was sliced 75 percent federal, 12.5 percent state, 12.5 percent local. This probably indicates that, in the nation's big tax grab, the prosperous urban industrial community fares even less well, relatively, than do other types of local communities. Yet these are the kinds of communities which have ever-growing needs for public services and facilities to serve the needs of their own people.

States and local governments can and will improve their services to and facilities for their citizens just as rapidly as conditions permit.

School Expenditures Increase

Proponents of the Federal Aid to Education bill, scheduled for immediate consideration by the 81st Congress, hold that $300,000,000 must be provided at once in federal grants to "save our schools". Opponents state that since this campaign to "save our schools" started twelve years ago, public school expenditures in the United States have risen from $1,760,000,000 in 1936 to an estimated $3,700,000,000 in

1948 - not a dime of which had to be provided by Uncle Sam.

Solution in cutting Tax Pie

Increased school population and the need for salary adjustments have intensified the school problem. Though teacher salaries on the average have caught up with the inflation parade, it is quite generally believed that pre-war scales were too low in many areas. To the extent that additional school funds may be needed, they could be much more soundly provided if the national tax pie were so cut as to give state and local governments larger slices than they are now getting. Federal overhead cost would be saved and the potentiality of federal control and federal concentration of power would diminish. Chart IV shows the extent to which the federal government has increased its share of the tax dollar in the past twenty years.

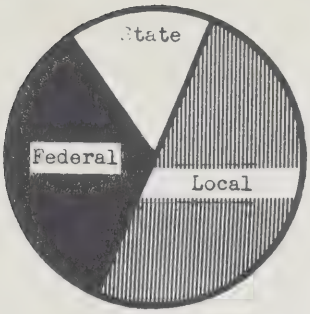
Returning to the Montgomery County tax survey, it may be pointed out that a reduction of only 4 percent in the 1947 federal tax collection would have left in the pockets of the County's taxpayers an aggregate sum equal to all the taxes paid that year to all the school districts of the County.

Savings from reduced federal taxes would, of course, not be immediately available for local government purposes under intricacies of our various tax systems, but if more money were left in Ohio and in Montgomery County, the state legislature and the local people could work out a means of taking adequate care of local facilities and services. Incidentally, there are no local community institutions in the country which generally command more loyalty, pride and support on the part of the local people than do the public schools.

Chart IV

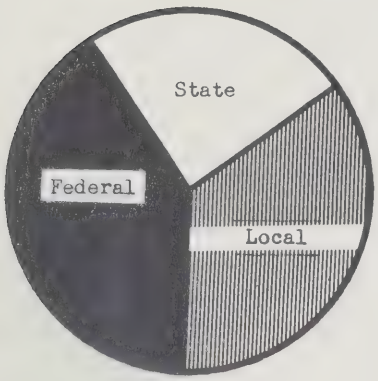
CHANGING PROPORTION OF FEDERAL, STATE AND LOCAL TAXATION

1928, 1938 and 1948



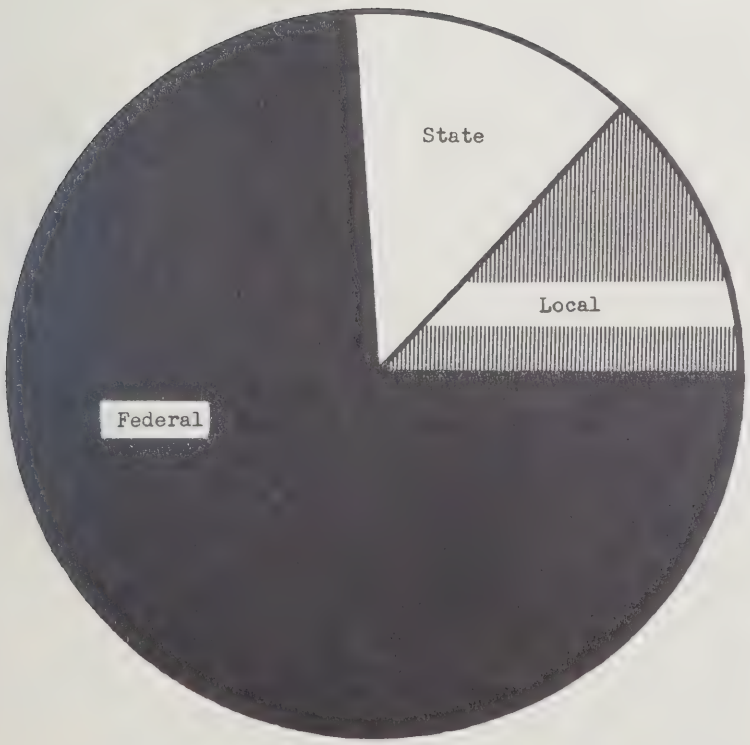
In 1928, the pie was $9,349,000,000

Federal slice -- 34%
State slice -- 16
Local slice -- 50



In 1938, the pie was $ 13,088,000,000

Federal slice -- 41%
State slice -- 24
Local slice -- 35



In 1948, the pie was $50,937,000,000

Federal slice -- 74%
State slice -- 13
Local slice -- 13

Source: Prepared from reports of the Department of Commerce and United States Treasury

The present system of slicing the national tax pie starves state and local facilities and services. The remedy is not to put them on a federal dole; it is to allow them to retain a larger slice of pie.

THE ROAD WE ARE TRAVELING

Array of Grants Amazing

In the preceding pages of this report, some indication has been given of the road along which we are moving toward heavier tax burdens, greater concentration of federal fiscal and administrative powers, and impairment of state rights and responsibilities. The grant-in-aid has become an important implement in the hands of those who would further these trends. As a conclusion to the present study, there is presented first, an exhibit showing the amazing array of federal grants for all manner of purposes, involving in many cases amounts so small as to make incomprehensible the acquiescence of the states in the principle and policy of federal aid. This is followed by data which show the rapidly mounting total of existing and projected grants.

The frittering away of resources through a multitude of small grants is illustrated in Table II[1/].

1/ From Annual Report of the Secretary of the Treasury, 1948, pp. 614-620. The total of federal grants shown in this table does not agree exactly with that given in the budget. The difference is probably produced by certain differences in accounting procedure in the Budget Bureau and in the Treasury, in which varying decisions may be made as to the classification of particular expenditure items.

TABLE II

Expenditures made in the fiscal year 1948 as Direct Payments to States

Purpose	Amount (000)
Department of Agriculture:	
Agricultural experiment stations-regular grants	$ 7,152
Agricultural extension work-regular grants	26,206
Forest fire cooperation-regular grants	9,094
National School lunch program-regular grants	65,116
Research and Marketing Act of 1946-regular grants	2,410
Exportation and domestic consumption of agricultural commodities	35,003
Supply and distribution of farm labor-emergency grants	591
Department of Commerce:	
Civil Aeronautics administration, federal airport program-regular	5,149
Department of the Interior:	
Federal aid, wildlife restoration, fish and wildlife-regular	2,521
Federal Security Agency:	
Office of Education:	
Colleges for agriculture and mechanic arts-regular	5,030
Cooperative vocational education	26,387
Public health service:	
Venereal disease control-regular	12,608
Tuberculosis control-regular	6,688
General health assistance-regular	11,173
Mental health activities-regular	1,653
Hospital survey and planning-regular	957
Children's bureau:	
Maternal and child health services-regular	10,584
Services for crippled children-regular	7,423
Child welfare services-regular	3,422
Social Security Administration:	
Emergency maternity and infant care-emergency	2,067
Old age assistance-regular	562,374
Aid to dependent children-regular	139,584
Aid to the blind-regular	16,401
Unemployment compensation-regular	67,722
American printing house for the blind-regular	125
Office of vocational rehabilitation-regular	21,688
Federal Works Agency:	
Bureau of Community Facilities:	
Public works advance planning-emergency	5,790
Veterans' educational facilities-emergency	51,236
Community facilities-emergency	1,142
Maintenance and operation of schools-emergency	4,118
Public Roads Administration:	
Highway construction-regular	303,066
" " -emergency	15,391
Liquidation of Public Works Administration-emergency	6,534
Housing and Home Finance Agency: Public Housing Administration	
Federal annual contributions-regular	3,336
Veterans' re-use housing program-emergency	41,590

TABLE II (cont.)

Department of Labor:	
Public employment offices-regular	$ 65,888
U.S. Maritime Commission:	
State marine schools-regular	153
Veteran's Administration:	
State and territorial homes for disabled soldiers and sailors-regular	1,732
Supervision of on-the-job training-regular	5,303
Administration of unemployment and self-employment allowances-regular	24,133
TOTAL	$1,578,543

In addition to the above outright grants, various sums are distributed as shared revenues. The Treasury report treats these as grants, which they are, but they are listed separately here to indicate the character of the revenue which is shared.

Shared Revenue Grants to States, 1948

Source	Amount (000)
Department of Agriculture:	
National forests fund	$ 4,626
Submarginal land program, payment to counties	390
Department of the Interior:	
Payments from receipts under mineral leasing act	5,664
Payments from receipts under migratory bird conservation act and Alaska game law	183
Payments under certain special acts	2,878
Department of the Army:	
Lease of flood control lands	207
Federal Power Commission:	
Payments to states under Federal Power Act	24
TOTAL SHARED REVENUES	$13,972

The shared revenues are of small consequence. For the most part, they consist of receipts from leases, from fees, and similar nontax sources.

The list of grants contains forty separate ways that have been devised to distribute federal money among the states. This list could

No Case for Smaller Grants

have been expanded to such length only on the assumption that the states have had to be coaxed into the adoption of various programs by the offer of a federal grant. The procedure is demoralizing and costly in relation to the results that can be accomplished from the distribution of the small amounts allotted under nearly all of the forty programs. The three social security programs - OAA, ADC, and AB (Old Age Assistance, Aid to Dependent Children, and Aid to the Blind) - and the regular highway construction grant account for roughly $1 billion of the total. More than a half billion dollars is scattered among thirty-six other programs, and there can be no pretense that any of the states would be unable to carry on any or all of these programs without the pittance which they receive from the federal government. The point is even stronger when federal administrative costs are considered.

Trend of Grants Upward

Turning from this portrayal of the "scattergun" grant-in-aid system, a summary of the trends and projections of estimated total expenditure is presented. An analysis of 1950 programs compared with those in effect in 1930 is attached, as Appendix B. Table III reveals the postwar pattern on a functional basis.

TABLE III
POSTWAR TREND PATTERN OF FEDERAL GRANTS-IN-AID
Source: U. S. Budget Reports
By fiscal years; figures in millions of dollars

Program categories	1947 Actual	1948 Actual	1949 Estimated	1950 Estimated
Veterans' service and benefits[1]	59	85	29	14
Social welfare, health and security[2,3]	866	892	1,156	1,359
Housing and community facilities[3]	394	54	25	13
Education and general research[3]	32	37	37	323
Agriculture and agricultural resources	65	64	62	63
Natural resources not primarily agricultural	10	11	21	18
Transportation and communication	208	334	470	518
Labor	43	133	130	138
TOTAL GRANTS[4]	1,670	1,610	1,930	2,446

1/ Part of an appropriation for a broader program.
2/ Excludes contract authorizations as follows: 1948, 75,000,000; 1949, 75,000,000; and 1950, 75,000,000.
3/ See Table IV.
4/ Excludes the federal contribution of $12,000,000 to the District of Columbia, which the Budget Bureau treats as a grant-in-aid.

State Chambers Project The Cost

The Council of State Chambers of Commerce has compiled a projection of the estimated costs of new spending programs which are contained in bills that have been introduced. To the extent that these pending proposals involve grants-in-aid, they should be regarded as supplemental to the budget figures. From the Council's study, the following data relative to new or expanded grants are taken:

TABLE IV

New Programs supplemental to those in the Budget for 1950

Purpose	Estimated Cost (millions) In 1950	Annual cost after 1950
Social Security:		
Increase of federal grants for OAA (see hearings)	a)	a)
A new formula for federal grants for public assistance	a)	a)
Slum clearance and housing	$210.5	$458.1 (40-yr. average to $545.0 high year)
Federal aid to education	290.0	$300.0 to $2,000.0
Survey of educational building needs and fellowships	1.00	
Construction of educational facilities	--	433.3
Grants for fellowships and scholarships		(no estimate)

a) An increase of $250 million annually in federal grants for old age assistance and home relief has been recommended by the Social Security Agency. Thus, the added cost of the new grant programs listed in Table IV, if all were adopted, would be $751.5 million in 1950, and in later years this cost would rise to $1,303.1 million, or as high as $3,003.1 million according to some estimates.

The Bill Grows

Table III presents budgeted estimates of federal grants totalling $2,446 million in 1950. The addition of the presently estimated costs of other new programs, in Table IV, raises the total cost of all grant programs to $3,197 million for that year. For subsequent years, the minimum annual cost of all programs now budgeted or proposed would be at least $3,700 million, with the possibility of an upper cost approximating $5,400 million.

The Illusion Persists

These should be sobering figures. They indicate that the Great Illusion still lives and flourishes, and that many persons still look upon the federal treasury as an inexhaustible source of free, costless money.

APPENDIX A

PER CAPITA INCOME INCREASES, 1940-1947

I. Wealthy States (per capita income equal or better than national average of $575 in 1940)

Rank		Per capita income increase, 1940-1947
1.	District of Columbia	50%
2.	Delaware	84
3.	New York	106
4.	Nevada	120
5.	Connecticut	102
6.	New Jersey	92
7.	California	104
8.	Massachusetts	89
9.	Illinois	124
10.	Rhode Island	113
11.	Maryland	105
12.	Michigan	119
13.	Ohio	124
14.	Washington	121
15.	Pennsylvania	118
16.	Wyoming	143
17.	Oregon	116
18.	Montana	186

The national per capita income increase from 1940 to 1947 was 130 percent.

Two states out of 18 in this group had per capita income increases greater than 130 percent.

II. Middle-income States (per capita income 75 to 99 percent of national average of $575 in 1940)

19.	New Hampshire	110
20.	Indiana	138
21.	Vermont	127
22.	Colorado	183
23.	Wisconsin	159
24.	Maine	122
25.	Minnesota	135
26.	Missouri	137
27.	Iowa	136
28.	Utah	152
29.	Florida	134
30.	Arizona	137
31.	Virginia	136
32.	Idaho	193
33.	Nebraska	186

12 states out of 15 in this group had per capita income increases greater than 130 percent.

III. Poorer States (per capita income less than 75 percent of national average of $575 in 1940)

34.	Kansas	212
35.	Texas	173
36.	West Virginia	159
37.	South Dakota	259
38.	North Dakota	356
39.	Louisiana	150
40.	New Mexico	196
41.	Oklahoma	161
42.	Georgia	181
43.	North Carolina	182
44.	Tennessee	189
45.	Kentucky	176
46.	South Carolina	172
47.	Alabama	212
48.	Arkansas	182
49.	Mississippi	226

All sixteen states of this group had per capita income increases greater than 130 percent.

APPENDIX B

GRANTS-IN-AID ESTIMATES FOR FISCAL YEAR 1950

(as estimated by the Bureau of the Budget)

A. Programs identical with 1930 programs, with figures for 1930 actual expenditures (R denotes regular grants, S denotes shared revenues)

Program	1930 Actual	1950 Estimated
Agricultural experiment stations (R)	$4,335,000	$ 7,406,208
Cooperative agricultural extension (R)	7,539,786	30,622,106
National forest fund (S)	1,565,032	5,995,000
National forest school fund (S)	41,243	55,000
Forest fire cooperation (R)	1,383,041	8,542,000
Forest planting stock (R)	80,315	---
Payments, mineral leasing (S)	1,387,838	9,600,000
" , 5% public lands (S)	18,292	---
" , Coos Bay (S)	43,613	19,000
" , Oregon counties (S)	979,387	2,500,000
" , Oklahoma (S)	41,778	4,000
Federal Power Commission (S)	12,875	26,700
Homes for soldiers and sailors (R)	575,206	3,100,000

Colleges for agricultural and mechanical arts (R)	2,550,000	5,030,000
Cooperative vocational education (R)	7,385,670	27,127,883
Vocational rehabilitation (R)	735,619	20,497,480
Education of the blind (R)	75,000	125,000
State marine schools (R)	50,000	300,000
Cooperative farm and forestry (R)	58,881	445,000
Maternal and child welfare (R)	9,522	23,106,205
National Guard (see footnote)	31,987.927	(242,000,000)*
Subtotals	$60,856,025	$386,501,582

* The item for National Guard was, in fact and in government accounting, a grants-in-aid-to-states item from its inception in 1916 through 1948. Since then the National Guard has been merged into the Army and is no longer, in fact or in government accounting, a grants-in-aid item. Since the expenditure continues, the item is shown here for comparative purposes, but is not included in the final 1950 total shown in the Table.

B. Public health programs in 1930 and 1950:

Program	1930 Actual	1950 Estimated
Epidemic control (R)	$ 273,330	----
Quarantine (R)	71,117	----
Rural sanitation (R)	345,159	----
Control of venereal disease	----	$ 13,520,000
" " tuberculosis	----	6,805,000
Assistance to states, general	----	22,000,000
Disease and sanitation investigation and control (Alaska)	----	360,000
Grants, hospital construction	----	60,000,000
Payments to states for surveys and programs for hospital construction	----	439,302
Mental health activities	----	3,250,000
Grants, National Heart Institute	----	300,000
" , National Cancer Institute	----	3,000,000
Grants and loans, water pollution control	----	1,000,000
Grants for plan preparation, water pollution control	----	450,000
Subtotals	$ 689,606	$111,124,302

C. Highway programs in 1930 and 1950:

Program	1930 Actual	1950 Estimated
Rural post roads	$77,887,693	----
Forest roads and trails	7,961,032	----
Federal-aid highway system	----	$ 7,000,000
Federal-aid secondary or feeder roads	----	4,000,000
Elimination of grade crossings	----	11,000,000
Federal-aid postwar construction program	----	440,000,000
Public lands highways	----	1,300,000
Strategic highway network (national defense)	----	2,000,000
Access roads (National defense)	----	3,300,000
Surveys and plans (national defense)	----	1,000,000
Emergency relief, highways, grade crossing elimination, etc.	----	500,000
Subtotals	$85,848,725	$470,100,000

D. Recapitulation of identical and comparable programs (A,B, & C above):

	1930 Actual	1950 Estimated
A.	$ 60,856,025	$386,501,582
B.	689,606	111,124,302
C.	85,848,725	470,100,000
1930 total and 1950 subtotal (including 1950 estimate for National Guard)	$147,394,356	$967,725,884

E. Programs started since 1930, on the basis of regular grants (starting dates in parentheses):

Program	1950 Estimated
Maintenance and operation of schools (anticipated supplemental) (1948)	$ 1,000,000
Research and Marketing Act (1946)	4,850,000
Exportation and domestic consumption of agricultural commodities (1936)	20,000,000
Wild life restoration (1937)	9,450,000
Airport program (1946)	47,250,000
Unemployment compensation administration (1935)	12,060
Unemployment compensation (1935)	135,006,440
Migratory bird conservation (1935)	100,000
Subtotal	$217,668,500

F. Programs started since 1930, on the basis of shared revenue (starting dates in parentheses):

Program	1950 Estimated
County payments on submarginal land (1937)	$ 233,200
Payments from grazing receipts (1934)	235,100
Dam payments to Arizona and Nevada (1938)	600,000
Flood control (1938)	243,750
TVA payments in lieu of taxes (1935)	2,200,000
Subtotal	$3,512,050

G. Programs started since 1930, on basis of emergency grants (starting dates in parentheses):

Program	1950 Estimated
Veterans' on-the-job training (1944)	$ 4,100,000
Veterans' unemployment and self-employment benefits (1944)	5,923,770
Veterans' educational facilities (1946)	516,000
Public assistance (1935)	1,063,000,000
National school lunch program (1946)	74,848,000
FWA liquidation (1944)	1,415,900
Low-rent housing, annual contributions (1937)	5,700,000
Veterans' re-use housing (1940)	604,100
Community facilities (defense public works) (1944)	500,000
Public works planning (1944)	6,000,000
Subtotal	$1,162,607,770

H. Estimated 1950 expenditures for future programs proposed in 81st Congress (1949):

Program	1950 Estimated
Extending public assistance	$ 65,000,000
Low-rent housing	500,000
Federal aid to education	290,000,000
Industrial safety	3,000,000
Subtotal	$358,500,000

I. Special program (not new, included in Budget Bureau list of grants-in-aid to States, but not in Treasury Department list):

District of Columbia, Federal contribution	$12,000,000

RECAPITULATION of 1950 estimated expenditures for federal grants-in-aid to states and local governments, as listed by the Bureau of the Budget.

Subtotal D (above)	$ 967,725,884
Deduct, 1950 estimate for National Guard (included above for purposes of comparison, but no longer operating on the grants-in-aid basis)	242,000,000
Balance of subtotal D	$ 725,725,884
Subtotal E	217,668,500
Subtotal F	3,512,050
Subtotal G	1,162,607,770
Subtotal H	358,500,000
Subtotal I	12,000,000
Budget Bureau Total	$2,480,014,204

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